

What are we doing anyway?

Deconstructing the terms that inform the field of market development

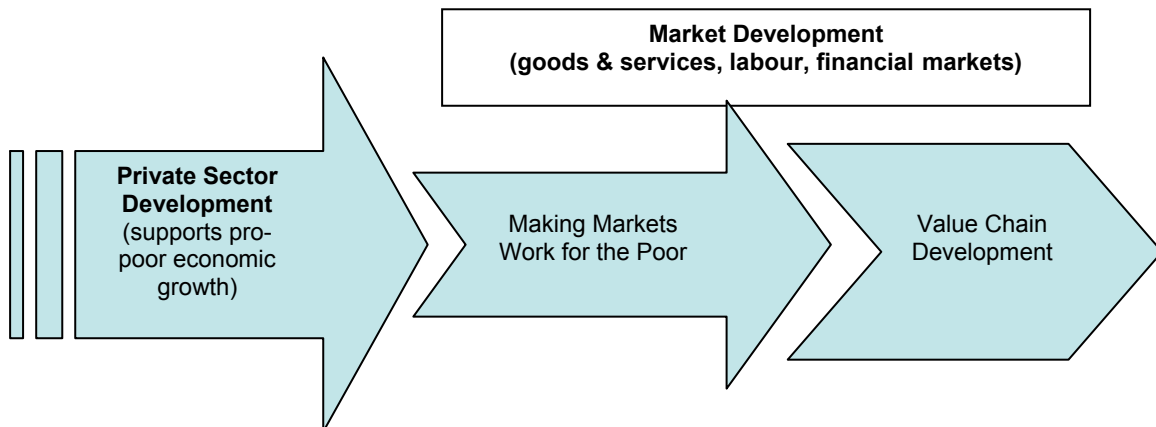
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Many of us working in the industry of development see the fallout of globalization when working with the world's poor. Export-oriented growth is seen as the main feature of economic development, and improving a country's global competitive position has become the foundation for this growth. There may be increased economic activity and employment, but economic returns decrease for various reasons, one being that the increase in exports often corresponds with lowering the wages of production so as a country can be competitive in the global marketplace. This results in negatively affecting income levels (Gereffi et al., 2001). In many countries the incidence of poverty has increased which has forced millions into the microenterprise sector in an attempt to earn a living.

MSEs and smallholder farmers do not operate in a vacuum: they operate within market systems which may be local, regional, or even international. When markets function well they can be efficient mechanisms for the exchange, coordination and allocation of resources, goods and services in an economy. Increasingly, international development initiatives that focus on economic growth and/or poverty alleviation are working to open existing markets to poor producers and consumers and make the benefits of well-functioning markets more widely accessible to the poor. These initiatives are enhancing the competitiveness of economies in developing countries by promoting private sector growth and MSE participation (McVay et al., 2005).

'These initiatives' are known as private sector development (PSD), market development, making markets work for the poor (MMW4P or M4P) and value chain development. How are these terms connected, what do they mean? This paper is an attempt to deconstruct the terms and illustrate how the approaches are all related.



Private Sector Development – PSD

Poverty reduction and sustainable economic development is required to achieve the first millennium development goal (MDG1) which is to reduce by half the proportion of people living on less than per day. Donors are in agreement that poverty reduction will only occur if there is a high rate of economic growth (OECD, 2004, Sida, 2004, UKGovernment, 2006, Downing et al., 2006).

Economic growth is generally accepted as a rise in gross domestic product (GDP) per capita. It is the private sector which takes the risk to invest and create wealth in market economies which in turn creates economic growth. And the private sector comprises of individuals, households and businesses. Poverty is commonly measured by the number of people, or the percentage of the population, who live below a defined poverty line. If the number of people below the poverty line decreases because their average income has increased, then poverty reduction would be achieved. Supporting private sector development is a means to stimulate economic growth.

If a country achieves economic growth and an increase in GDP, this does not necessarily indicate that poverty reduction has occurred. Economic growth that favours the poor (known as pro poor growth) is achieved when economic growth benefits the poor as farmers, micro enterprise operators, as employees, as consumers and as recipients of tax funded services like education and health (Downing et al., 2006, OECD, 2004). If the poor are not able to take advantage of the opportunities that have arisen out of the growth in the economy and access markets as consumers, suppliers or labourers, the poor will not benefit from the growth.

The old agenda for donor supported private sector development use to focus on providing support to small enterprises and agribusinesses which provided livelihoods for the poor. Experience has shown that it is market outcomes that actually improve the income of the poor, not specific types of enterprises. *The new agenda for pro poor private sector development is concerned with the rate of economic growth as well as the opportunities for the poor and the degree to which the poor can take advantage of the opportunities and benefit with improved incomes* (OECD, 2004).

Private sector development is the overall strategy to achieve sustainable economic growth with poverty reduction. Economic growth that benefits the poor requires institutions and policies which open up opportunities for the poor to access markets.

Market Development

Well functioning markets can be a mechanism for the distribution of goods and services in an economy. They can reduce the cost of doing business and encourage foreign investment which often results in economic growth. Yet as development practitioners know, economic growth does not necessarily result in higher incomes for people living in poverty or contribute towards poverty reduction. *The participation of the poor in markets as buyers and sellers, and the terms of their participation, indicate whether economic growth is pro-poor or not.*

If markets are going to work better for people living in poverty, input and output markets need to provide them with access to opportunities to build and acquire assets, and assist in reducing vulnerability. Market development which benefits the poor is about using

market systems to meet the needs of people living in poverty and supporting private sector development through market mechanisms. Its objective is to increase the competitiveness of manufacturing and agricultural industries in which large numbers of micro and small enterprises (MSEs) participate and understands that the interests of the smallest firms in an industry is interdependent with the performance of the whole industry. This requires that the contribution of MSEs needs to increase which by default will increase the benefits to MSEs. IF the industry is going to improve its competitiveness, then MSEs need to improve their competitiveness. This more often than not requires that they upgrade and that the enabling environment is improved to facilitate their entry.

Pro-poor market development focuses on private sector development which benefits people living in poverty as consumers and buyers. Pro poor market development looks at ALL the final markets in which MSEs CAN sell and the chain of events (inputs-production-distribution-wholesaling-retailing) that occur to a product or service to reach these final markets.

Making Markets Work for the Poor (M4P) is a market development approach that has been developed by European Donors to develop market systems which benefit the poor. The development of value chains is a means to operationalize pro poor market development to strengthen specific market systems which will benefit the poor as suppliers and improve their incomes. USAID has been the leader in developing tools to conduct value chain analysis, and the Donors in Europe incorporate the value chain in their market development work.

Making Markets Work for the Poor (MMW4P/M4P)

The concept of M4P emerged in the late 1990's with some European Donors (DFID, SIDA, GTZ) and the Asian Development Bank. It is a framework to analyze and respond to how markets can work better for the poor as suppliers and consumers. This framework combines an analysis of poverty based sustainable livelihoods model¹ with an analyses of the functioning of markets based on insights from new institutional economics (NIE) (DFID, 2005).

NIE questions the relevance of the neo classical assumption that markets are perfect mechanisms for controlling distribution because information is signalled through the price system. This insinuates that price information is available to all actors. NIE takes the position that information is incomplete, asymmetrical (not equally available to all) and costly to acquire. Acquiring information and covering the risk of doing business when information cannot be relied upon, increases transaction costs. The increased risks and costs to participate in markets can cause market failure which is when goods and services are not distributed efficiently by the market.

A little bit the about the livelihoods framework

The livelihoods framework has been informed by a social development perspective which starts by exploring assets and strategies that households and communities employ to survive in vulnerable environments. Power relations are studied as well as the manner in which cash is used in the household. This framework has traditionally been household focussed. Within the M4P framework, the household is analyzed in relation to input and output market opportunities for the household economy.

In NIE, institutions are the 'rules of the game' which shape economic behaviour. These institutions can be formal (laws, trade agreements, standards, etc) or informal (social, religious or cultural) (North, 1980). Markets are institutions which organize the exchange

¹ See <http://www.livelihoods.org/> for more information on the DFID's livelihoods framework.

of goods and services in a manner which reduces risks and transaction costs. M4P adapts the NIE analysis of markets which emphasizes the role of institutions and the level of 'transaction costs' in influencing economic behaviour. For markets to work for the poor they must provide access to the opportunity to build and acquire assets and help reduce vulnerability (DFID, 2005).

Social or economic barriers to entry in the market may exclude segments of the population—ethnic and tribal groups, migrants, women, landless, HIV/AIDS affected households, remote communities. M4P addresses market failure resulting from formal and informal institutions that prohibit the poor from accessing labour markets, land and markets for goods and services (Albu, 2007).

M4P focuses on the macro-level constraints that prevent markets from working—the formal institutions also known as the business enabling environment—and uses the value chain approach to strengthen market systems in which the poor operate.

Value Chain Development

Michael Porter developed the value chain as a tool of analysis to determine and enhance the competitive advantage of a firm within an industry (Porter, 1985). The value chain is a diagnostic tool that disaggregates a firm into discrete activities which it performs in the production of a product. These activities are designing, producing, marketing and distributing the product to reach the final consumer. Development studies has taken the value chain concept from business management and has adapted it to look the journey of a product from producer to consumer across borders and continents to determine the barriers to entry for the poor, coordination requirements and the horizontal and vertical linkages necessary between firms (Kaplinsky, 2000). USAID has been the leader in the value chain approach which is reflected in their commitment of resources to develop tools for value chain analysis and assessing the impact of value chain projects.

A value chain is the sequence of activities that transforms a product or service from an idea to a product to reach a distinct consumer market. The value of the product increases at each point in the process of transformation. More value is added to the product along this chain of activities to meet the specific desires and needs of a higher-value market.

MSEs often operate in a value chain where the market channel targets consumers who are poor. This may be because their product is of poor quality, or they do not have access to transportation and other market outlets, or they do not have access to technology to add value to their product. Reducing the transaction costs or increasing the revenue of the poor participating in value chains as suppliers or buyers addresses market failure and stimulates private sector development.

Value-chain analysis can help to assess MSE competitiveness, market opportunities for MSEs, and the factors that compromise their capacity to participate in higher value markets. The analysis reveals:

- End market opportunities at the local, national and global levels
- Inter-firm cooperation – vertical and horizontal relationships
- Existence of markets that support business performance – examples being finance, communications, transportation, information & technical assistance

- The enabling environment at the national, regional and global level

The existing tools to conduct a value chain analysis do not incorporate an analysis of informal institutions which regulate markets and often exclude segments of the population. Inter-firm relations are affected by power dynamics that are established by socio-cultural traditions. These traditions may exclude a tribe or ethnic group or the participation of women in interfacing in the market. In very weak and fragile markets, especially post conflict, the elements of what constitutes trust in business relations is critical to rebuilding market channels. An understanding of the formal and informal institutions that shape economic behaviour in markets can strengthen a value chain analysis and result in sustainable pro poor market development.

Conclusion

Private sector development that promotes pro poor growth is at the top of the agenda for donors. Pro poor growth is measured by the reduction in numbers of people who live below the poverty line. In order for this to occur, the poor need to increase their incomes. And for the average incomes of the poor to increase, they need accessible opportunities in labour, input and output markets.

When the private sector develops, markets develop and when markets develop, the private sector develops. Ensuring that there is pro poor growth requires the development of markets which benefit the poor as suppliers and consumers.

Making markets work for the poor (M4P) is an approach influenced by new institutional economics (NIE) which asserts that formal (laws, regulations, treaties, etc) and informal (culture, traditions, mores, etc) institutions affect economic behaviour and the functioning of markets. Its objective is to develop markets that benefit the poor as consumers and suppliers by addressing the barriers to entry for the poor.

The value chain is a diagnostic tool to analyze end market opportunities, the upgrading needs of firms, the horizontal and vertical business linkages and the business enabling environment. This tool originated in business management and focuses on determining the competitive advantage of firms within their industry. It has been adapted by development practitioners to identify market systems where the poor can reach higher value markets and design projects that remove the constraints that prohibit entry into these markets. Developing value chains that benefit the poor is a means to develop pro poor markets and achieve pro poor private sector development.

Table 1: Comparison between M4P and Value Chain Approaches

	M4P	Value Chain
Theoretical foundation	New Institutional Economics	Business Management Literature
Champions	<ul style="list-style-type: none"> • DFID • ABD • SwissContact • SIDA 	USAID
Orienting concepts	<ul style="list-style-type: none"> • Formal and informal Institutions • Exclusion • Market Embeddedness 	<ul style="list-style-type: none"> • Business Enabling Environment • Upgrading • Horizontal & Vertical Linkages- Governance • Firm competitiveness
Intellectual influences	<ul style="list-style-type: none"> • Douglass North 	<ul style="list-style-type: none"> • Michael Porter

Understanding the relations between PSD, MD, PPMD (pro poor market development), M4P and value chains can help us as practitioners to communicate better with donors and to understand where we fit in the overall development equation.

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